

DOUGLAS DYNAMICS, INC
Form 10-Q
November 08, 2010
[Table of Contents](#)

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

Form 10-Q

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2010

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____.

Commission file number: 001-34728

DOUGLAS DYNAMICS, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

134275891
(I.R.S. Employer
Identification No.)

7777 North 73rd Street

Milwaukee, Wisconsin 53223

(Address of principal executive offices) (Zip code)

(414) 354-2310

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐

Non-accelerated filer ☒
(Do not check if a smaller reporting company)

Accelerated filer ☐

Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

Number of shares of registrant's common shares outstanding as of November 8, 2010 was 21,405,426

Table of Contents

DOUGLAS DYNAMICS, INC.

Table of Contents

<u>PART I. FINANCIAL INFORMATION</u>	1
<u>Item 1. Financial Statements</u>	1
Unaudited Consolidated Balance Sheets as of September 30, 2010 and December 31, 2009	1
Unaudited Consolidated Statements of Operations for the three and nine months ended September 30, 2010 and 2009	2
Unaudited Consolidated Statements of Cash Flows for the nine months ended September 30, 2010 and 2009	3
Notes to Unaudited Consolidated Financial Statements	4
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	13
Item 3. Quantitative and Qualitative Disclosures About Market Risk	24
Item 4. Controls and Procedures	25
<u>PART II. OTHER INFORMATION</u>	25
<u>Item 1. Legal Proceedings</u>	25
<u>Item 1A. Risk Factors</u>	25
Item 2. Unregistered Sales of Equity Securities, Use of Proceeds and Issuer Purchases of Equity Securities	32
Item 3. Defaults Upon Senior Securities	33
Item 4. (Removed and Reserved)	33
Item 5. Other Information	33
Item 6. Exhibits	33
Signatures	34

[Table of Contents](#)**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****Douglas Dynamics, Inc.****Consolidated Balance Sheets****(In thousands except share data)**

	September 30, 2010 (unaudited)	December 31, 2009 (audited)
Assets		
Current assets:		
Cash and cash equivalents	\$ 8,721	\$ 69,073
Accounts receivable, net	82,397	32,172
Inventories	24,475	26,697
Deferred income taxes	3,729	3,729
Prepaid income taxes	6,596	-
Prepaid management fees-related party	-	417
Prepaid and other current assets	1,336	1,446
Total current assets	127,254	133,534
Property, plant, and equipment, net	22,183	26,661
Assets held for sale	1,854	--
Goodwill	107,222	107,222
Other intangible assets, net	128,328	132,950
Deferred financing costs, net	1,084	3,311
Other long-term assets	941	941
Total assets	\$ 388,866	\$ 404,619
Liabilities, redeemable stock and stockholders equity		
Current liabilities:		
Accounts payable	\$ 6,545	\$ 5,170
Accrued expenses and other current liabilities	12,097	12,598
Accrued interest	30	5,367
Income taxes payable	-	1,202
Short-term borrowings	37,000	--
Current portion of long-term debt	1,250	850
Total current liabilities	56,922	25,187
Retiree health benefit obligation	7,801	7,848
Pension obligation	8,926	8,957
Deferred income taxes	22,367	18,913
Deferred compensation	1,669	1,482
Long-term debt, less current portion	120,575	231,813
Other long-term liabilities	2,110	2,195

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

Redeemable preferred stock - Series A, par value \$0.01, 65,000 shares authorized, no shares outstanding at September 30, 2010 and December 31, 2009	-	-
Redeemable preferred stock - Series B, par value \$0.01, no shares outstanding at September 30, 2010 and one share outstanding at December 31, 2009	-	1
Redeemable preferred stock - Series C, par value \$0.01, no shares outstanding at September 30, 2010 and one share outstanding at December 31, 2009	-	1

Stockholders' equity:

Common Stock, par value \$0.01, 200,000,000 shares authorized at September 30, 2010, 23,750,000 authorized at December 31, 2009, 21,405,426 and 14,421,736 shares issued and outstanding at September 30, 2010 and December 31, 2009, respectively	214	144
Additional paid-in capital	126,831	59,973
Stockholders' notes receivable	(478)	(1,013)
Retained earnings	45,729	53,055
Accumulated other comprehensive loss, net of tax	(3,800)	(3,937)
Total stockholders' equity	168,496	108,222
Total liabilities, redeemable stock and stockholders' equity	\$ 388,866	\$ 404,619

See the accompanying notes to consolidated financial statements

Table of Contents**Douglas Dynamics, Inc.****Consolidated Statements of Operations****(In thousands, except share and per share data)**

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 30,	September 30,
	2010	2009	2010	2009
	(unaudited)		(unaudited)	
Net sales	\$ 47,448	\$ 50,396	\$ 128,338	\$ 125,206
Cost of sales	32,221	35,241	86,070	87,523
Gross profit	15,227	15,155	42,268	37,683
Selling, general, and administrative expense	6,819	4,916	20,527	15,443
Intangibles amortization	1,541	1,541	4,621	4,621
Management fees-related party	57	411	6,370	1,066
Income from operations	6,810	8,287	10,750	16,553
Interest expense, net	(2,334)	(3,802)	(9,038)	(11,756)
Loss on extinguishment of debt	-	-	(7,967)	--
Other expense, net	(12)	(22)	(7)	(105)
Income (loss) before taxes	4,464	4,463	(6,262)	4,692
Income tax expense (benefit)	2,279	1,725	(2,803)	751
Net income (loss)	\$ 2,185	\$ 2,738	\$ (3,459)	\$ 3,941
Weighted average number of common shares outstanding:				
Basic	21,158,573	14,421,736	17,963,720	14,424,347
Diluted	21,546,767	14,747,041	17,963,720	14,749,652
Earnings (loss) per share:				
Basic	\$ 0.10	\$ 0.19	\$ (0.19)	\$ 0.27
Diluted	\$ 0.10	\$ 0.19	\$ (0.19)	\$ 0.27
Cash dividends declared & paid per share	\$ 0.18	\$ 0.00	\$ 0.18	\$ 0.00

See the accompanying notes to consolidated financial statements.

Table of Contents

Douglas Dynamics, Inc.

Consolidated Statements of Cash Flows

(in thousands)

	Nine Months Ended	
	September 30, 2010	September 30, 2009
	(unaudited)	
Operating activities		
Net income (loss)	\$ (3,459)	\$ 3,941
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	9,448	8,498
Amortization of deferred financing costs	741	853
Loss on extinguishment of debt	7,967	--
Stock-based compensation	3,158	738
Provision for losses on accounts receivable	281	116
Deferred income taxes	3,374	133
Changes in operating assets and liabilities:		
Accounts receivable	(50,446)	(53,901)
Inventories	2,222	1,949
Prepaid and other assets and prepaid income taxes	(6,069)	(245)
Accounts payable	1,375	(43)
Accrued expenses and other current liabilities	(7,268)	(2,742)
Deferred compensation	187	187
Benefit obligations and other long-term liabilities	54	633
Net cash used in operating activities	(38,435)	(39,883)
Investing activities		
Capital expenditures	(2,414)	(4,821)
Proceeds from sale of equipment	212	--
Net cash used in investing activities	(2,202)	(4,821)
Financing activities		
Stock repurchases	(2)	(1,000)
Payment of call premium and post payoff interest on senior notes redemption	(3,876)	--
Collection of stockholders' notes receivable	535	--
Payments of financing costs	(2,605)	--
Revolver borrowings	37,000	10,000
Proceeds from initial public offering, net	63,938	--
Borrowings on long-term debt	40,000	--
Dividends paid	(3,867)	--
Repayment of long-term debt	(150,838)	(638)
Net cash provided by (used in) financing activities	(19,715)	8,362
Change in cash and cash equivalents	(60,352)	(36,342)

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

Cash and cash equivalents at beginning of period		69,073		53,552
Cash and cash equivalents at end of period	\$	8,721	\$	17,210

See the accompanying notes to consolidated financial statements.

Table of Contents

Douglas Dynamics, Inc.

Notes to Unaudited Consolidated Financial Statements

(in thousands except share and per share data)

1. Description of business and basis of presentation

Douglas Dynamics, Inc., is the North American leader in the design, manufacture and sale of snow and ice control equipment for light trucks, which is comprised of snowplows and sand and salt spreaders, and related parts and accessories. The Company's snow and ice control products are sold through a network of over 720 truck equipment distributors that purchase directly from the Company and are located throughout the snowbelt regions in North America (primarily the Midwest, East and Northeast regions of the United States as well as all provinces of Canada). The Company sells its products under the WESTERN®, FISHER®, and BLIZZARD® brands. The Company is headquartered in Milwaukee, WI and as of September 30, 2010 had manufacturing facilities in Milwaukee WI, and Rockland, ME. The Company completed the closure of its Johnson City, TN facility, in the quarter ending September 30, 2010. The Company operates as a single segment.

All share and per share data reported herein have been retrospectively restated to reflect the 23.75-for-one stock split of the Company's common stock that occurred on May 7, 2010, immediately prior to the consummation of the Company's initial public offering (IPO).

Initial Public Offering

On May 10, 2010, the Company completed its IPO of 10,000,000 shares of common stock at a public offering price of \$11.25 per share, less underwriting discounts. The 10,000,000 shares sold included 6,500,000 shares sold by the Company and 3,500,000 shares sold by certain selling stockholders. In addition, on May 14, 2010, the selling stockholders in the IPO closed the sale of an additional 1,500,000 shares to the underwriters at the public offering price of \$11.25 per share, less underwriting discounts, pursuant to the underwriters' exercise in full of their overallotment option. The Company received \$73,125 in gross proceeds from the issuance and sale of its common stock in the IPO and \$63,938 in net proceeds after deducting underwriting discounts and total expenses related to the offering. The Company did not receive any proceeds from the sale of its stock by the selling stockholders in the IPO.

Capitalization summary upon closing of IPO:

Common stock issued and outstanding at December 31, 2009	14,421,736
Issuance and sales of common stock by Company through IPO	6,500,000
Issuance of non-vested common stock in connection with IPO	208,130
Shares issued for options exercised in connection with IPO	180,567
Fractional shares repurchased and retired in connection with IPO	(7)

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

Common stock issued and outstanding upon closing of IPO

21,310,426

Concurrent with the closing of the IPO, the Company repurchased its one issued and outstanding share of Series B preferred stock and one issued and outstanding share of Series C preferred stock, each at a price of \$1,000 per share. Subsequent to the repurchase of the preferred stock, the Company has no preferred stock outstanding.

Summary of Significant Accounting Policies

The Company's significant accounting policies are disclosed in its audited consolidated financial statements for the year ended December 31, 2009, included in the Prospectus dated May 6, 2010 and have not changed materially as of September 30, 2010.

Interim Consolidated Financial Information

The accompanying consolidated balance sheet as of September 30, 2010 and the consolidated statements of operations for the three and nine months ended September 30, 2010 and 2009 and cash flows for the nine months ended September 30, 2010 and 2009 have been prepared by the Company and have not been audited. In the opinion of management, all adjustments, consisting of only normal recurring adjustments necessary for the fair presentation of the financial position, results of operations and cash flows, have been made. Pursuant to the rules and regulations of the Securities and Exchange Commission certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted from the accompanying interim consolidated financial statements. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the consolidated financial statements for the year ended December 31, 2009.

Table of Contents

Other comprehensive income (loss) includes the net income (loss) of the Company plus the Company's adjustments for its defined benefit retirement plans based on the measurement date as of the Company's year end. Other comprehensive income (loss) was \$2,185 and \$(3,322) for the three and nine months ended September 30, 2010, respectively. Other comprehensive income was the same as net income for the three and nine months ended September 30, 2009, respectively.

The Company's business is seasonal and consequently its results of operations and financial condition vary from quarter-to-quarter. In addition, because of this seasonality, the Company's results of operations for any quarter may not be indicative of results of operations that may be achieved for a subsequent quarter or the full year, and may not be similar to results of operations experienced in prior years. The Company attempts to manage the seasonal impact of snowfall on its revenues in part through its pre-season sales program. This pre-season sales program encourages the Company's distributors to re-stock their inventory during the second and third quarters in anticipation of the peak fourth quarter retail sales period by offering favorable pre-season pricing and payment deferral until the fourth quarter. As a result, the Company tends to generate its greatest volume of sales during the second and third quarters. By contrast, its revenue and operating results tend to be lowest during the first quarter as management believes the Company's end-users prefer to wait until the beginning of a snow season to purchase new equipment and as the Company's distributors sell off inventory and wait for the pre-season sales incentive period to re-stock inventory. Fourth quarter sales vary from year-to-year as they are primarily driven by the level, timing and location of snowfall during the quarter. This is because most of the Company's fourth quarter sales and shipments consist of re-orders by distributors seeking to restock inventory to meet immediate customer needs caused by snowfall during the winter months.

Fair value measurements

The Company adopted the guidance originally issued in FASB statement No. 157, *Fair Value Measurements* (codified in Accounting Standards Codification (ASC) 820-10, *Fair Value Measurements and Disclosures*) (ASC 820-10) on January 1, 2008. ASC 820-10, among other things, defines fair value, establishes a consistent framework for measuring fair value, and expands disclosure for each major asset and liability category measured at fair value on either a recurring basis or nonrecurring basis. ASC 820-10 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, the pronouncement establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows: (Level 1) observable inputs such as quoted prices in active markets; (Level 2) inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and (Level 3) unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

Assets and liabilities measured at fair value are based on the market approach, which is prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. At September 30, 2010 and December 31, 2009, the Company did not have any financial instruments accounted for at fair value.

Principles of consolidation

The accompanying consolidated financial statements include the accounts of Douglas Dynamics, Inc. and its direct wholly-owned subsidiary, Douglas Dynamics, L.L.C., and its indirect wholly-owned subsidiaries, Douglas Dynamics Finance Company and Fisher, L.L.C. (hereinafter collectively referred to as the Company). All intercompany balances and transactions have been eliminated in consolidation.

Use of estimates

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Accordingly, actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to prior year financial statements to conform to the current year presentation.

Table of Contents**2. Fair Value**

The carrying values of the Company's cash and cash equivalents (Level 1), trade accounts receivable, accounts payable, accrued expenses and short term borrowings approximated fair value as of September 30, 2010. The fair value of the Company's long-term debt, including current maturities, is estimated using discounted cash flows based on the Company's current incremental borrowing rates for similar types of borrowing arrangements. The carrying value and fair value (Level 2) of the Company's long-term debt at September 30, 2010 was \$121,825 and \$120,607, respectively.

3. Inventories

Inventories consist of the following:

	September 30, 2010	December 31, 2009
Finished goods and work-in-process	\$ 23,087	\$ 24,639
Raw material and supplies	1,388	2,058
	\$ 24,475	\$ 26,697

4. Property, plant and equipment

Property, plant and equipment are summarized as follows:

	September 30, 2010	December 31, 2009
Land	\$ 960	\$ 1,000
Land improvements	1,768	2,218
Buildings	11,030	13,766
Machinery and equipment	21,662	23,092
Furniture and fixtures	6,128	6,934
Mobile equipment and other	982	969
Construction-in-process	2,374	4,252
Total property, plant and equipment	44,904	52,231
Less accumulated depreciation	(22,721)	(25,570)
Net property, plant and equipment	\$ 22,183	\$ 26,661

5. Long-Term Debt

Long-term debt is summarized below:

	September 30, 2010	December 31, 2009
Term Loan	\$ 121,825	\$ 82,663
Senior notes	-	150,000
Total long-term debt	121,825	232,663
Less current maturities	1,250	850
	\$ 120,575	\$ 231,813

Table of Contents

As of December 31, 2009, the Company's senior credit facilities consisted of an \$85,000 term loan facility and a \$60,000 revolving credit facility with a group of banks and the Company also had outstanding \$150,000 of 7.75% senior notes (the "Senior Notes") due January 15, 2012. Concurrent with the consummation of the IPO, the Company amended its senior credit facilities to, among other things, (i) allow it to redeem the Senior Notes, (ii) increase the size of its term loan facility by \$40,000 and (iii) amend certain of the provisions in its senior credit facilities which govern the Company's ability to pay dividends. Consequently, at September 30, 2010, the Company's senior credit facilities consist of a \$125,000 term loan facility and a \$60,000 revolving credit facility with a group of banks. In connection with the amendments to the Company's senior credit facilities, the interest on the existing portion of the term loan facility was revised. The change consisted of an increase from an interest rate equal to (at the Company's option) either the base rate plus 1.25% or the eurodollar rate plus 2.25% to (at the Company's option) either the base rate (which shall be no less than 3%) plus 3.5% or the eurodollar rate (which shall be no less than 2%) plus 4.5%. The interest for the additional \$40,000 increase in the Company's term loan facility is an interest rate equal to (at the Company's option) either the base rate (which shall be no less than 3%) plus 4% or the eurodollar rate (which shall be no less than 2%) plus 5%. Under the revolving credit facility, the margin for base rate loans is either 0.25% or 0.50% and the margin for eurodollar rate loans is either 1.25% or 1.50%, in each case determined based on the Company's leverage ratio from time to time. The amendment of the term loan facility resulted in a significant modification of the debt which resulted in the write off of unamortized capitalized deferred financing costs of \$995 and expenditures of \$2,046 related to financing costs paid to existing lenders which was recorded as a loss on extinguishment of debt in the consolidated statements of operations for the nine months ended September 30, 2010. As the amendment of the term loan facility occurred in the three month period ended June 30, 2010, there was no additional write off of deferred financing costs or expenditures relating to financing costs in the three month period ended September 30, 2010.

On June 9, 2010, the Company completed the redemption of its Senior Notes. The Company redeemed its Senior Notes with the proceeds from the additional term loan, together with the net IPO proceeds and cash on hand for a total of \$157,557, which includes \$3,681 of interest that accrued through the date of deposit with the trustee, \$969 of interest that accrued from the date of deposit with the trustee to the date of redemption and a \$2,907 redemption call premium of 1.938%. In addition, the Company wrote off \$1,050 of unamortized deferred financing costs related to the Senior Notes.

After effecting the discharge of the Senior Notes, the maturity date for the Company's revolving credit facility is May 21, 2012, and the Company's term loan amortizes in nominal amounts quarterly with the balance payable on May 21, 2013 with respect to the existing term loans and May 21, 2016 with respect to the additional term loans.

At September 30, 2010 the Company had outstanding borrowings on the revolving credit facility of \$37,000 and remaining borrowing availability of \$22,976.

The Company's senior credit facilities include certain negative and operating covenants, including restrictions on its ability to pay dividends, and other customary covenants, representations and warranties and events of default. The senior credit facilities entered into and recorded by the Company's subsidiaries significantly restrict its subsidiaries from paying dividends and otherwise transferring assets to Douglas Dynamics, Inc. The terms of the Company's revolving credit facility specifically restrict subsidiaries from paying dividends if a minimum availability under the revolving credit facility is not maintained (such event, a "liquidity event"), and both senior credit facilities restrict subsidiaries from paying dividends above certain levels or at all if an event of default has occurred. In addition, the Company's revolving credit facility includes a requirement that, subject to certain exceptions, capital expenditures may not exceed \$10,000 in any calendar year and, during the occurrence of a liquidity event, that the Company comply with a monthly minimum fixed charge coverage ratio test of 1.0:1.0. Compliance with the fixed charge coverage ratio test is subject to certain cure rights under the Company's revolving credit facility. At September 30, 2010, the Company was in compliance with the respective covenants. The credit facilities are collateralized by substantially all assets of the Company.

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

In accordance with the senior credit facilities, the Company is required to make additional principal prepayments over the above scheduled payments under certain conditions. This includes, in the case of the term loan facility, 100% of the net cash proceeds of certain asset sales, certain insurance or condemnation events, certain debt issuances, and, within 150 days of the end of the fiscal year, 50% of excess cash flow, as defined, including a deduction for allowed distributions (which percentage is reduced to 25% or 0% upon the achievement of certain leverage ratio thresholds), for any fiscal year. Excess cash flow is defined in the senior credit facilities as consolidated adjusted EBITDA (earnings before interest, taxes, depreciation and amortization) plus a working capital adjustment less the sum of repayments of debt and capital expenditures subject to certain adjustments, interest and taxes paid in cash, management fees and certain restricted payments (including dividends or distributions). Working capital adjustment is defined in the senior credit facilities as the change in working capital, defined as current assets excluding cash and cash equivalents less current liabilities excluding current portion of long term debt. As of September 30, 2010 and December 31, 2009, the Company was not required to make an excess cash flow payment.

Table of Contents**6. Accrued Expenses and Other Liabilities**

Accrued expenses and other liabilities are summarized as follows:

	September 30, 2010	December 31, 2009
Payroll and related costs	\$ 2,847	\$ 3,659
Employee benefits	2,699	2,534
Accrued warranty	3,039	3,040
Other	3,512	3,365
	\$ 12,097	\$ 12,598

7. Warranty Liability

The Company accrues for estimated warranty costs as sales are recognized and periodically assesses the adequacy of its recorded warranty liability and adjusts the amount as necessary. The Company's warranties generally provide, with respect to its snow and ice control equipment, that all material and workmanship will be free from defect for a period of two years after the date of purchase by the end-user, and with respect to its parts and accessories purchased separately, that such parts and accessories will be free from defect for a period of one year after the date of purchase by the end-user. Certain snowplows only provide for a one year warranty. The Company determines the amount of the estimated warranty costs (and its corresponding warranty reserve) based on the Company's prior five years of warranty history utilizing a formula driven by historical warranty expense and applying management's judgment. The Company adjusts its historical warranty costs to take into account unique factors such as the introduction of new products into the marketplace that do not provide a historical warranty record to assess. The warranty reserve is included in Accrued Expenses and Other Current Liabilities in the accompanying consolidated balance sheets.

The following is a rollforward of the Company's warranty liability:

	Three months ended September 30, 2010	September 30, 2009	Nine months ended September 30, 2010	September 30, 2009
Balance at the beginning of the period	\$ 2,489	\$ 1,824	\$ 3,040	\$ 2,272
Warranty provision	721	851	1,775	1,956
Claims paid/settlements	(171)	(165)	(1,776)	(1,718)
Balance at the end of the period	\$ 3,039	\$ 2,510	\$ 3,039	\$ 2,510

Table of Contents**8. Employee Retirement Plans**

The components of net periodic pension cost consist of the following:

	Three months ended		Nine months ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Component of net periodic pension cost:				
Service cost	\$ 200	\$ 205	\$ 600	\$ 615
Interest cost	358	338	1,074	1,016
Expected return on plan assets	(290)	(246)	(870)	(738)
Amortization of net loss	81	130	243	390
Net periodic pension cost	\$ 349	\$ 427	\$ 1,047	\$ 1,283

The Company estimates its total required minimum contributions to its pension plans in 2010 will be \$1,050. Through September 30, 2010, the Company has made \$711 of cash contributions to the pension plans in 2010 versus \$1,179 through the same period 2009.

In May 2010, in connection with the closure of the Company's manufacturing facility in Johnson City, TN substantially all the employees at this facility were terminated. This resulted in a cessation of all future benefit accruals for these employees under the Company's pension and other post employment benefit (OPEB) plans. A curtailment gain of \$366 was recognized as a reduction to the net actuarial loss, as the curtailment liability gain was less than the unrecognized net actuarial loss prior to the curtailment for the pension plan. Therefore, this did not impact the consolidated statement of operations for the nine months ended September 30, 2010.

Components of net periodic other postretirement benefit cost consist of the following:

	Three months ended		Nine months ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Components of net periodic other postretirement benefit cost				
Service cost	\$ 71	\$ 76	\$ 237	\$ 229
Interest cost	107	105	348	315
Amortization of net (gain)/loss	--	(18)	(7)	(55)
Curtailment gain - Johnson City location closing	--		(667)	
Net periodic other postretirement benefit cost	\$ 178	\$ 163	\$ (89)	\$ 489

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

The curtailment gain for the OPEB plan exceeded the unrecognized net actuarial loss prior to the curtailment and resulted in a gain of \$1,031 of which \$667 was recorded in selling, general and administrative expense in the consolidated statement of operations for the nine months ended September 30, 2010 and \$364 (before taxes) was recognized as a reduction to the net actuarial loss in accumulated other comprehensive loss at September 30, 2010. As the curtailment occurred in the three month period ending June 30, 2010, there was no impact on the statement of operations for the three month period ending September 30, 2010.

Table of Contents**9. Dividends**

Cash dividends declared and paid on a per share basis were as follows:

	Three and nine months ended September 30,			
	2010		2009	
Dividends declared	\$	0.18	\$	0.00
Dividends paid	\$	0.18	\$	0.00

10. Stock Repurchases

On January 23, 2009, the Company entered into securities repurchase agreements with certain members of management. Pursuant to these agreements, the Company repurchased at fair value and subsequently retired 27,004 shares of common stock and 89,371 stock options in exchange for aggregate consideration of \$1,137, comprised of a cash payment of \$1,000 and the satisfaction of the remaining principal amount of \$137 on promissory notes held by the members of management. As a result of the repurchase of stock options, the Company recorded \$738 of compensation expense in the nine months ended September 30, 2009, which represented the fair value of the repurchased options.

11. Earnings Per Share

Basic earnings per share of common stock is computed by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted earnings per share of common stock is computed by dividing net income (loss) by the weighted average number of shares of common stock and common stock equivalents and assumed exercise of stock options, using the treasury stock method as well as the conversion of both class A and class B restricted shares. Stock options for which the exercise price exceeds the average fair value and restricted shares have an anti-dilutive effect on earnings per share and are excluded from the calculation. There were 458,770 shares excluded from diluted earnings per share for the nine months ended September 30, 2010 as the shares would be anti-dilutive for that period as the Company incurred a net loss.

The following shares were used to calculate basic and diluted earnings per share for the periods presented.

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Basic weighted average common shares outstanding	21,158,573	14,421,736	17,963,720	14,424,347
	388,194	325,305	-	325,305

Incremental shares applicable to common stock
options and restricted stock

Average diluted weighted average common shares outstanding	21,546,767	14,747,041	17,963,720	14,749,652
---	------------	------------	------------	------------

12. Employee Stock Plans

Amended and Restated 2004 Stock Incentive Plan

In connection with the IPO, in May 2010, the Company's Board of Directors and stockholders amended and restated the Company's 2004 Stock Incentive Plan (as amended and restated, the "A&R 2004 Plan") and certain outstanding award agreements thereunder, to among other things, eliminate the ability of the holders thereunder to use a promissory note to pay any portion of the exercise price of the options, to provide that the use of net exercises to pay any portion of the exercise price of the options shall be at the sole discretion of the committee administering the A&R 2004 Plan, and to effect certain ministerial changes under the A&R 2004 Plan. In addition, in connection with the IPO, the Board of Directors also resolved not to issue any further awards under the A&R 2004 Plan. As of September 30, 2010, 356,044 shares of common stock are reserved for issuance upon the exercise of outstanding options under the A&R 2004 Plan. All outstanding options are fully vested, excluding 47,500 options, of which 23,750 will vest on August 27, 2011 and the remaining options will vest on August 27, 2012. All options expire 10 years from the date of grant.

Table of Contents

2010 Stock Incentive Plan

In connection with the IPO, in May 2010, the Company's Board of Directors and stockholders adopted the 2010 Stock Incentive Plan (the "2010 Plan"). The 2010 Plan provides for the issuance of nonqualified stock options, incentive stock options, stock appreciation rights, restricted stock awards and restricted stock units, any of which may be performance-based, and for incentive bonuses, which may be paid in cash or stock or a combination of both, to eligible employees, officers, non-employee directors and other service providers to the Company and its subsidiaries. A maximum of 2,130,000 shares of common stock may be issued pursuant to all awards under the 2010 Plan.

In May 2010, in connection with the IPO, an aggregate of 208,130 shares of restricted stock were granted to certain officers and employees under the 2010 Plan. The restricted stock awards were time-based and vest over a five-year period in equal annual installments of 20% per year, commencing on the first anniversary of the grant date. The restricted stock does not carry voting or dividend rights until the stock vests.

As of September 30, 2010, the Company had 1,921,870 shares of common stock available for future issuance of awards under the 2010 Plan. The shares of common stock to be issued under the 2010 Plan will be made available from authorized and unissued Company common stock.

Stock Options

The following table summarizes information with respect to the Company's stock option activity under the A&R 2004 Plan for the three and nine months ended September 30, 2010. In connection with the IPO, certain of the Company's selling stockholders exercised 288,570 stock options and sold the underlying shares. Such stockholders paid the exercise price of such options through a net exercise. In the three months ending September 30, 2010, certain of the Company's selling stockholders exercised 174,571 stock options and paid the exercise price of such options through a net exercise, resulting in an additional 95,000 outstanding shares. The options exercised in conjunction with the IPO as well as those exercised in the three month period ending September 30, 2010 were granted under APB 25 with an exercise price equal to fair value at date of grant, and accordingly no compensation expense was recorded at the time of grant. As a result of the net exercise mechanism, the optionholders did not bear the risk and rewards of the options. As such, the Company recorded \$1,227 and \$2,975 of stock based compensation expense for the three and nine months ended September 30, 2010 respectively. The following is a rollforward of stock option activity for the three and nine months ended September 30, 2010.

	Three months ended September 30, 2010	Nine months ended September 30, 2010
Stock options - beginning of period	530,615	819,185
Options exercised	(174,571)	(463,141)
Stock options - end of period	356,044	356,044

Restricted Stock Awards

A summary of restricted stock activity for the nine months ended September 30, 2010 is as follows:

	Shares (In thousands)	Weighted Average Grant Date Fair value	Weighted Average Remaining Contractual Term
Unvested at December 31, 2009			
Granted	208,130	\$ 11.25	4.59 years
Vested			
Cancelled and forfeited			
Unvested at September 30, 2010	208,130	\$ 11.25	4.59 years
Expected to vest in the future at September 30, 2010	208,130	\$ 11.25	4.59 years

Table of Contents

The fair value of the Company's restricted stock awards is the closing stock price on the date of grant, or \$11.25 per share. The Company recognized \$110 and \$183 of compensation expense related to restricted stock awards granted for the three and nine months ended September 30, 2010. The unrecognized compensation expense calculated under the fair value method for shares expected to vest as of September 30, 2010 was approximately \$1,707 and is expected to be recognized over a weighted average period of 4.59 years.

13. Commitments and Contingencies

In the ordinary course of business, the Company is engaged in various litigation including product liability and intellectual property disputes. However, the Company does not believe that any pending litigation will have a material adverse effect on its consolidated financial position. In addition, the Company is not currently a party to any environmental-related claims or legal matters.

14. Restructuring

On April 27, 2009, the Company announced a plan to close its Johnson City, TN manufacturing facility and move production from this facility to its Milwaukee, WI and Rockland, ME facilities. The company completed the closure of this facility as of August 31, 2010. The Company expects to realize significant annual cost savings and improved customer delivery performance as a result. The closure has resulted in the elimination of approximately 100 positions in Johnson City and the addition of approximately 50 positions in Rockland and approximately 35 positions in Milwaukee.

Related to the facility closure, the Company recorded (\$46) and \$78 of employee termination costs and \$45 and \$750 for other closure costs for the three and nine months ended September 30, 2010, respectively. Restructuring expenses of \$872 and \$897 were recorded for the three and nine months ended September 30, 2009, respectively. The Company expects the total cost of this restructuring to be \$2,103 consisting of employee termination costs of \$768 and other costs of \$1,335. The other costs consist principally of facility move preparation and equipment relocation costs. These costs are included in the selling, general and administrative expense line in the Company's consolidated statements of operations.

The following represents a reconciliation of changes in the restructuring reserves related to this project through September 30, 2010.

	Employee Termination Costs	Other Exit Costs	Total
Accrued restructuring reserves as of December 31, 2009	\$ 690	\$ -	\$ 690
Activity during nine months ended September 30, 2010:			
Charges to earnings	78	750	828
Payments	(700)	(750)	(1,450)
Accrued restructuring reserves as of September 30, 2010	\$ 68	\$ -	\$ 68

In connection with the restructuring, the Company reassessed the useful lives of its manufacturing facility and certain equipment. As a result of this assessment, the Company assigned shorter useful lives to these assets and recorded accelerated depreciation of \$447 and \$1,877 for the three and nine months ended September 30, 2010, respectively. This change in estimate reduced basic and diluted earnings per share by \$0.01 and \$0.06 for the three and nine months ended September 30, 2010, respectively. The Company did not record any accelerated depreciation for the three and nine months ended September 30, 2009. Because of actions taken in the restructuring, the Johnson City property is being actively marketed for sale in the third quarter of fiscal 2010 and is classified as held for sale in the consolidated balance sheet.

15. Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The largest item affecting deferred taxes is the difference between book and tax amortization of goodwill and other intangibles amortization. The Company estimates that the effective combined federal and state tax rate for 2010 will be approximately 43%. The Company's effective tax

Table of Contents

rate was 51.1% and 38.7% for the three months ended September 30, 2010 and 2009, respectively. The Company's effective tax rate (benefit) for the nine months ended September 30, 2010 and 2009 was (44.8%) and 16.0%, respectively. The effective tax rate (benefit) for the nine months ended September 30, 2010 was higher than the corresponding period in 2009 due to the release of a valuation allowance for Wisconsin net operating losses (NOLs) in the first quarter of 2009 due to a tax law change in the state of Wisconsin resulting in the ability to utilize the NOLs in future periods.

16. Related Party Transactions

The Company is party to a Joint Management Services Agreement with Aurora Management Partners, LLC (AMP) and ACOF Management, LP (ACOF), affiliates of its principal stockholders. Prior to the IPO, this agreement obligated the Company to pay an annual management fee of \$1,250 per annum, to AMP and ACOF, pro rata in accordance with their respective holdings, plus reimbursement of reasonable out-of-pocket expenses, in exchange for consultation and advice in fields such as financial services, accounting, general business management, acquisitions, dispositions and banking.

In connection with the Company's IPO, the Company amended and restated the terms of its Joint Management Services Agreement to, among other things, (i) extend the term of service until the earlier of (A) the fifth anniversary of the consummation of the Company's IPO, (B) such time as AMP and ACOF, together with their affiliates, collectively hold less than 5% of the Company's outstanding common stock and (C) such time as all parties mutually agree in writing, while eliminating all other termination events (other than termination for cause); (ii) eliminate the annual management fee, as well as the provision obligating the Company to pay AMP and ACOF a transaction fee in the event of an acquisition or any sale or disposition of the Company or any of its divisions or any sale of substantially all Company assets or similar transactions in exchange for a one-time fee of \$5,800 upon the consummation of the IPO, pro rata in accordance with their respective holdings; and (iii) modify the expense reimbursement provisions to include reimbursement for out-of-pocket expenses incurred in connection with SEC and other legally required filings made by each of AMP and ACOF with respect to the Company's securities and certain other expenses. The one-time management fee was paid on May 10, 2010, and is included in management fees related party expense for the nine months ended September 30, 2010.

During the three and nine months ended September 30, 2010, the Company recognized management fees and related expenses of \$57 and \$6,370 respectively relating to the Joint Management Service Agreement. For the three and nine months ended September 30, 2009 the Company recognized \$411 and \$1,066, respectively, relating to the Joint Management Services Agreement.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes which are included in Item 1 of this Quarterly Report on Form 10-Q, as well as the information contained in the prospectus related to our initial public offering (IPO), dated May 4, 2010, filed with the Securities and Exchange Commission (SEC) in accordance with Rule 424(b) of the Securities Act of 1933, as amended (the Securities Act) on May 6, 2010, which is accessible on the SEC's website at www.sec.gov.

In this Quarterly Report on Form 10-Q, unless the context indicates otherwise: Douglas Dynamics, the Company, we, our, or us refer to Douglas Dynamics, Inc. (formerly known as Douglas Dynamics Holdings, Inc.).

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains certain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). These statements include information relating to future events, product demand, the payment of dividends, future financial performance, strategies, expectations, closure of our Johnson City manufacturing facility, competitive environment, regulation and availability of financial resources. These statements are often identified by use of words such as anticipate, believe, intend, estimate, expect, continue, should, could, may, plan, project, predict, will and similar expressions and include references to assumptions and relate to our future prospects, developments and business strategies. Such statements involve known and unknown risks, uncertainties and other factors that could cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to: (i) weather conditions, particularly lack of or reduced levels of snowfall; (ii) a significant decline in economic conditions; (iii) our inability to maintain good relationships with our distributors; (iv) lack of available or favorable financing options for our end-users or distributors; (v) increases in the price of steel or other materials necessary for the production of our products that cannot be passed on to our distributors; (vi) the inability of our suppliers to meet our volume or quality requirements; (vii) our inability to protect or continue to build our intellectual property portfolio; (viii) our inability to develop new products or improve upon existing products in response to end-user needs; (ix) losses due to lawsuits arising out of personal injuries

Table of Contents

associated with our products; and (x) our inability to compete effectively against competition, as well as those discussed in the section entitled Risk Factors, set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q. Given these risks and uncertainties, you should not place undue reliance on these forward-looking statements. In addition, the forward-looking statements in this Quarterly Report on Form 10-Q speak only as of the date hereof and we undertake no obligation, except as required by law, to update or release any revisions to any forward-looking statement, even if new information becomes available in the future.

Our Business

We are the North American leader in the design, manufacture and sale of snow and ice control equipment for light trucks, which consists of snowplows and sand and salt spreaders, and related parts and accessories. We sell our products under the WESTERN®, FISHER® and BLIZZARD® brands which are among the most established and recognized in the industry. We believe that in 2009 our share of the light truck snow and ice control equipment market was greater than 50%. We sell our products exclusively through what we believe is the industry's most extensive North American distributor network, which primarily consists of over 720 truck equipment distributors who purchase directly from us and are located throughout the snowbelt regions in North America (primarily the Midwest, East and Northeast regions of the United States as well as all provinces of Canada). We have longstanding relationships with many of our distributors, with an average tenure of approximately 15 years. We continually seek to grow and optimize our network by opportunistically adding high-quality, well-capitalized distributors in select geographic areas and by cross-selling our industry-leading brands within our distribution network. Beginning in 2005, we began to extend our reach to international markets, establishing distribution relationships in Northern Europe and Asia, where we believe meaningful growth opportunities exist.

The annual demand for snow and ice control equipment is driven primarily by the replacement cycle of the existing installed base, which is predominantly a function of the average life of a snowplow or spreader and is driven by usage and maintenance practices of the end-user. We believe actively-used snowplows are typically replaced, on average, every 7 to 8 years. The primary factor influencing the replacement cycle for snow and ice control equipment is the level, timing and location of snowfall.

Accordingly, our sales depend primarily on the level, timing and location of snowfall. Sales of our products in any given year and region are most heavily influenced by local snowfall levels in the prior snow season. Heavy snowfall during a given winter causes usage of our equipment to increase, resulting in greater wear and tear and shortened life cycles, thereby creating a need for replacement equipment and additional parts and accessories. In addition, when there is a heavy snowfall in a given winter, the increased income our professional snowplowers generate from their professional snowplow activities provides them with increased purchasing power to purchase replacement snow and ice control equipment prior to the following winter. Moreover, in our experience, the timing of snowfall in a given winter also influences our end-users decision-making process. Because an early snowfall can be viewed as a sign of a heavy upcoming snow season, our end-users may respond to an early snowfall by purchasing replacement snow and ice control equipment earlier than they might otherwise have. Alternatively, light snowfall during a given winter season may cause equipment usage to decrease, thereby extending its useful life and delaying replacement equipment purchases. Because the level, timing and location of snowfall are critical drivers of our sales, our results of operations vary from year-to-year and from season-to-season as snowfall varies from year-to-year. See Seasonality and Year-to-Year Variability and Risk Factors. The year-to-year variability of our business can cause our results of operations and financial condition to be materially different from year-to-year; whereas the seasonality of our business can cause our results of operations and financial condition to be materially different from quarter-to-quarter. While snowfall levels vary within a given year and from year-to-year, snowfall, and the corresponding replacement cycle of snow and ice control equipment, is relatively consistent over multi-year periods.

The demand for our snow and ice control equipment can also be influenced by general economic conditions in the United States, as well as local economic conditions in the snowbelt regions in North America. In stronger economic conditions, our end-users may choose to replace or upgrade existing equipment before its useful life has ended, while in weak economic conditions, our end-users may seek to extend the useful life

of equipment, thereby increasing the sales of parts and accessories. While our parts and accessories yield slightly higher gross margins than our snow and ice control equipment, they yield significantly lower revenue than equipment sales, which adversely affects our results of operations. However, since snow and ice control management is a non-discretionary service necessary to ensure public safety and continued personal and commercial mobility in populated areas that receive snowfall, end-users cannot extend the useful life of snow and ice control equipment indefinitely and must replace equipment that has become too worn, unsafe or unreliable, regardless of economic conditions.

Costs of Sales and Selling, General and Administrative Expense

Our costs of sales consist primarily of variable costs, including labor, materials and manufacturing overhead. Our selling, general and administrative expenses consist primarily of our expenses for general administration, sales, marketing, advertising, administration, incentive plans and intangible amortization. Because of our highly variable cost structure, we are able to easily reduce our costs of sales during periods following a year in which snowfall levels were low and during periods in which sales are lower. Our selling, general and administrative expenses can also be reduced temporarily in such periods to maximize cash flow.

Table of Contents

Although steel is a significant component of our cost of sales, we attempt to mitigate increases in the price of steel by implementing corollary price increases for our products in the form of a permanent price increase (in circumstances in which we believe the increase in the price of steel will be permanent) or temporary surcharges (in circumstances in which we believe the increase in the price of steel will be temporary).

Initial Public Offering

On May 10, 2010, the Company completed its IPO of 10,000,000 shares of common stock at a public offering price of \$11.25 per share, less underwriting discounts. The 10,000,000 shares sold included 6,500,000 shares sold by the Company and 3,500,000 shares sold by certain selling stockholders. In addition, on May 14, 2010, the selling stockholders in the IPO closed the sale of an additional 1,500,000 shares to the underwriters at the public offering price of \$11.25 per share, less underwriter discounts, pursuant to the underwriters' exercise in full of their over-allotment option. The Company received approximately \$73.1 million in gross proceeds from the issuance and sale of its common stock in the IPO and approximately \$63.9 million in net proceeds after deducting underwriting discounts and total expenses related to the IPO. The Company did not receive any proceeds from the sale of its stock by the selling stockholders in the IPO. The Company used the proceeds from the IPO, together with the increase in its term loan facility and cash on hand, to redeem all of its outstanding \$150.0 million, 7.75% senior notes ("Senior Notes") due January 15, 2012, including accrued and unpaid interest thereon and the related redemption premium.

Closure of Johnson City, Tennessee Manufacturing Facility

During the third quarter of 2010, the Company completed the closure its Johnson, City, Tennessee manufacturing facility. The Company ceased substantially all manufacturing at this facility on April 2, 2010, effectively reducing its manufacturing facilities from three to two, and ceased all operations at this facility as of August 31, 2010. In connection with the cessation of substantially all manufacturing at its Johnson City facility, in May 2010 substantially all of the employees at the facility were terminated. The closure resulted in the elimination of approximately 100 positions in Johnson City and the addition of approximately 50 positions in Rockland and approximately 35 positions in Milwaukee. The Company continues to own its Johnson City, Tennessee real property, which is being actively marketed for sale.

Results of Operations

Overview

During the three months ended September 30, 2010 and 2009, we sold 13,085 and 13,847 units of snow and ice control equipment, respectively, and during the nine months ended September 30, 2010 and 2009, we sold 32,491 and 31,315 units of snow and ice control equipment, respectively. The following table shows our sales of snow and ice control equipment and related parts and accessories as a percentage of net sales for the three and nine months ended September 30, 2010 and 2009.

Three months ended		Nine months ended	
September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

Equipment	91%	91%	87%	85%
Parts and accessories	9%	9%	13%	15%

The following table sets forth, for the three and nine months ended September 30, 2010 and 2009, the consolidated statements of operations of Douglas Dynamics, Inc. and its subsidiaries. All intercompany balances and transactions have been eliminated in consolidation. In the table below and throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, consolidated statements of operations data for the three and nine months ended September 30, 2010 and 2009 have been derived from our unaudited consolidated financial statements. The information contained in the table below should be read in conjunction with our consolidated financial statements and the related notes included elsewhere in this Quarterly Report on Form 10-Q.

Table of Contents

	Three Months Ended		Nine Months Ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
	(unaudited)		(unaudited)	
	(in thousands)			
Net sales	\$ 47,448	\$ 50,396	\$ 128,338	\$ 125,206
Cost of sales	32,221	35,241	86,070	87,523
Gross profit	15,227	15,155	42,268	37,683
Selling, general, and administrative expense	6,819	4,916	20,527	15,443
Intangibles amortization	1,541	1,541	4,621	4,621
Management fees-related party	57	411	6,370	1,066
Income from operations	6,810	8,287	10,750	16,553
Interest expense, net	(2,334)	(3,802)	(9,038)	(11,756)
Loss on extinguishment of debt	-	-	(7,967)	-
Other expense, net	(12)	(22)	(7)	(105)
Income (loss) before taxes	4,464	4,463	(6,262)	4,692
Income tax (benefit) expense	2,279	1,725	(2,803)	751
Net income (loss)	\$ 2,185	\$ 2,738	\$ (3,459)	\$ 3,941

Table of Contents

The following table sets forth for the three and nine months ended September 30, 2010 and 2009, the percentage of certain items in our consolidated statement of operations, relative to net sales:

	Three Months Ended		Nine Months Ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
	(in thousands)			
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	67.9%	69.9%	67.1%	69.9%
Gross profit	32.1%	30.1%	32.9%	30.1%
Selling, general, and administrative expense	14.4%	9.8%	16.0%	12.3%
Intangibles amortization	3.2%	3.1%	3.6%	3.7%
Management fees-related party	0.1%	0.8%	4.9%	0.9%
Income from operations	14.4%	16.4%	8.4%	13.2%
Interest expense, net	(5.0)%	(7.5)%	(7.1)%	(9.4)%
Loss on extinguishment of debt	0.0%	0.0%	(6.2)%	0.0%
Other expense, net	0.0%	0.0%	(0.0)%	(0.1)%
Income (loss) before taxes	9.4%	8.9%	(4.9)%	3.7%
Income tax (benefit) expense	4.8%	3.5%	(2.2)%	0.6%
Net income (loss)	4.6%	5.4%	(2.7)%	3.1%

Net Sales

Net sales were \$47.4 million for the three months ended September 30, 2010 compared to \$50.4 million in the three months ended September 30, 2009, a decrease of \$3.0 million, or 6.0%. The pre-season sales period is comprised of the second and third quarters combined. To encourage distributors to receive shipments prior to the peak fourth quarter retail selling season, we offer promotional financial and freight terms to distributors that place orders during the second quarter. These orders are then shipped during the second and third quarters. The timing of these shipments between the second and third quarters can vary year to year based upon a number of factors, including distributor inventory levels and space availability. For 2010, pre-season orders have shifted from traditional patterns to be more heavily weighted toward the second quarter versus the third quarter. Net sales were \$128.3 million for the nine months ended September 30, 2010 compared to \$125.2 million in the nine months ended September 30, 2009, an increase of \$3.1 million, or 2.5%. The decrease in net sales for the three months ended September 30, 2010 was driven by a decrease in units of 5.5% and a reduction in parts and accessories sales for the three-month period of \$0.3 million, or 5.3%. The increase in net sales for the nine months ended September 30, 2010 was driven by a 3.8% increase in unit sales of snow

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

and ice control equipment, due in part to above average snowfall during the October 1, 2009 to March 31, 2010 snow season and improving retail sales in February and March of 2010. Slightly offsetting this increase was a reduction in parts and accessories sales for nine months ended September 30, 2010 compared to the corresponding period in 2009 of \$1.7 million, or 8.4%, as end-users opted to purchase replacement equipment instead of repairing existing equipment.

Cost of Sales

Cost of sales were \$32.2 million for the three months ended September 30, 2010 compared to \$35.2 million for the three months ended September 30, 2009, a decrease of \$3.0 million, or 8.5%. Cost of sales were \$86.1 million for the nine months ended September 30, 2010 compared to \$87.5 million for the nine months ended September 30 2009, a decrease of \$1.4 million, or 1.7%. The decreases in cost of sales for the three and nine months ended September 30, 2010 compared to the corresponding period in 2009 were driven by changes in unit sales as discussed above under *Net Sales* . Slightly offsetting the decrease in cost of sales due to lower units was non-recurring accelerated depreciation costs totaling \$0.5 million and \$1.9 million, respectively, associated with

Table of Contents

reassessing the useful lives of the Company's manufacturing facilities and certain equipment at our Johnson City plant. Cost of sales decreased at a higher rate than net sales due to lower material costs than in the prior comparable periods. As a percentage of cost of sales, fixed and variable costs were approximately 16% and 84%, respectively, for the three months ended September 30, 2010 versus approximately 15% and 85%, respectively, for the three months ended September 30, 2009, and approximately 20% and 80%, respectively, for the nine months ended September 30, 2010 versus approximately 17% and 83%, respectively, for the nine months ended September 30, 2009.

Gross Profit

Gross profit was \$15.2 million for the three months ended September 30, 2010 compared to \$15.2 million in the three months ended September 30, 2009, an increase of \$0.1 million, or 0.5%. Gross profit was \$42.3 million for the nine months ended September 30, 2010 compared to \$37.7 million in the nine months ended September 30, 2009, an increase of \$4.6 million, or 12.2%. Gross profit dollars remained relatively flat for the three month period due to a decrease in units sold offset by lower cost of sales as a percentage of net sales. As a percentage of net sales, gross profit increased from 30.1% for the three months ended September 30, 2009 to 32.1% for the corresponding period in 2010. The increase in gross profit for the nine months ended September 30, 2010 was due primarily to the increased units sales of snow and ice control equipment described above under Net Sales. As a percentage of net sales, gross profit increased from 30.1% for the nine months ended September 30, 2009 to 32.9% for the corresponding period in 2010, primarily as a result of the factors discussed above under Net Sales and Cost of Sales.

Selling, General and Administrative Expense

Selling, general and administrative expenses, including intangible amortization and management fees, were \$8.4 million for the three months ended September 30, 2010, compared to \$6.9 million for the three months ended September 30, 2009, an increase of \$1.5 million. Selling, general and administrative expenses were \$31.5 million for the nine months ended September 30, 2010, compared to \$21.1 million for the nine months ended September 30, 2009, an increase of \$10.4 million. This increase for the three months ended September 30, 2010 was primarily due to compensation expense associated with net exercises of stock options totaling \$1.2 million and an increase in legal fees of \$0.3 million. In addition to the increases noted in the three-month period, the increase for the nine months ended September 30, 2010 was primarily attributable to non-recurring expenses incurred at the time of the Company's IPO. The non-recurring charges associated with the IPO totaled \$8.5 million, and were comprised namely of the buyout of the management services agreement at \$5.8 million, compensation expense associated with net exercises of stock options totaling \$1.7 million and the expense and payment of cash bonuses under the Company's liquidity bonus plan of \$1.0 million. As a percentage of net sales, selling, general and administrative expenses increased to 17.7% for the three months ended September 30, 2010 compared to 13.7% for the corresponding period in 2009, and from 16.9% for the nine months ended September 30, 2009 to 24.6% for the corresponding period in 2010, due to the factors discussed above.

Interest Expense

Interest expense was \$2.3 million for the three months ended September 30, 2010 compared to \$3.8 million in the corresponding period in 2009, a decrease of \$1.5 million. Interest expense was \$9.0 million for the nine months ended September 30, 2010 compared to \$11.8 million in the corresponding period in 2009, a decrease of \$2.8 million. This decrease in interest expense for the three and nine months ended September 30, 2010 was due to less interest expense as a result of the redemption of the Senior Notes with proceeds from the IPO, additional borrowings under the Company's senior credit facilities and cash on hand.

Loss On Extinguishment of Debt

Loss on extinguishment of debt totaling \$8.0 million for the nine months ended September 30, 2010 was entirely driven by costs associated with the amendment of our senior credit facilities and the redemption of the Senior Notes, including both the call premium on the redemption of our Senior Notes, and the write-off of unamortized deferred financing costs relating to the redemption of our Senior Notes and the amendment of our senior credit facilities.

Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The largest item affecting deferred taxes is the difference between book and tax amortization of goodwill and other intangibles amortization. The Company estimates that the Company's effective combined federal and state tax rate for 2010 will be approximately 43%. The Company's effective tax rate was 51.1% and 38.7% for the three months ended September 30, 2010 and 2009, respectively. The Company's effective tax rate for the nine months ended September 30, 2010 and 2009 was (44.8)% and 16.0%, respectively. The effective tax rate (benefit) for the nine months ended September 30, 2010 was higher than the corresponding period in 2009 due to the release of a valuation allowance for Wisconsin NOLs in the first quarter of 2009 due to a tax law change in the state of Wisconsin resulting in the ability to utilize the NOLs in future periods.

Table of Contents

Net Income (Loss)

Net income for the three months ended September 30, 2010 was \$2.2 million compared to net income of \$2.7 million for the corresponding period in 2009, a decrease of \$0.5 million. Net loss for the nine months ended September 30, 2010 was \$3.5 million compared to net income of \$3.9 million for the corresponding period in 2009, a decrease of \$7.4 million. This decrease in net income was driven by the factors described above and primarily by the impact of non-recurring costs incurred at the time of the Company's IPO. See the reconciliation table of Net Income (Loss) to Adjusted Net Income in Non-GAAP Financial Measures below for more details regarding the non-recurring expenses. As a percentage of net sales, net income was 4.6% for the three months ended September 30, 2010 compared to 5.4% for the three months ended September 30, 2009. As a percentage of net sales, net loss was 2.7% for the nine months ended September 30, 2010 compared to net income of 3.1% for the nine months ended September 30, 2009.

Adjusted EBITDA

Adjusted EBITDA for the three months ended September 30, 2010 was \$11.6 million compared to \$12.7 million in the corresponding period in 2009, a decrease of \$1.1 million, or 8.7%. Adjusted EBITDA for the nine months ended September 30, 2010 was \$32.1 million compared to \$28.0 million in the corresponding period in 2009, an increase of \$4.1 million, or 14.6%. As a percentage of net sales, Adjusted EBITDA decreased from 25.1% for the three months ended September 30, 2009 to 24.4% for the three months ended September 30, 2010, and increased from 22.4% for the nine months ended September 30, 2009 to 25.0% for the nine months ended September 30, 2010. For the three-month period ending September 30, the decrease in Adjusted EBITDA is primarily attributable to decreased unit sales of snow and ice control equipment. For the nine-month period ending September 30, the increase in EBITDA is primarily attributable to increased unit sales of snow and ice equipment which resulted from stronger pre-season shipments during the second quarter of 2010 compared to the corresponding period in 2009.

Non-GAAP Financial Measures

This Quarterly Report on Form 10-Q contains financial information calculated other than in accordance with U.S. generally accepted accounting principles (GAAP).

These non-GAAP measures include:

- Adjusted net income; and
- Adjusted EBITDA.

These non-GAAP disclosures should not be construed as an alternative to the reported results determined in accordance with GAAP.

Adjusted net income represents net income as determined under GAAP, excluding non-recurring expenses incurred at the time of our IPO, namely the buyout of our management services agreement, the loss on extinguishment of debt, stock based compensation expense associated with the net exercise of stock options and the payment of cash bonuses under our liquidity bonus plan. We believe that the presentation of Adjusted net income for the three and nine months ended September 30, 2010 provides useful information to investors by facilitating comparisons to our historical performance due to the non-recurring expenses incurred at the time of the our IPO in May 2010.

Table of Contents

The following table presents a reconciliation of net income (loss), the most comparable GAAP financial measure, to adjusted net income for the three and nine months ended September 30, 2010. There were no such adjustments during the three and nine months ended September 30, 2009.

	Three Months Ended	Nine Months Ended
(in millions)	September 30, 2010	September 30, 2010
Net Income (Loss) - (GAAP)	\$2.2	(\$3.5)
Addback non-recurring expenses, net of tax at 43.0%, incurred at the time of the IPO:		
- Buyout of the Management Services Agreement	-	\$3.3
- Loss on extinguishment of debt	-	\$4.6
- Liquidity bonus payment	-	\$0.6
- Non-recurring stock based compensation expense	\$0.7	\$1.7
Adjusted Net Income - (non-GAAP)	\$2.9	\$6.7

Adjusted EBITDA represents net income (loss) before interest, taxes, depreciation and amortization, as further adjusted for management fees paid by us to affiliates of our principal stockholders, stock-based compensation associated with the net exercise of stock options, payment of cash bonuses under our liquidity bonus plan, loss on extinguishment of debt, certain non-recurring charges related to the closure of our Johnson City, Tennessee manufacturing facility and certain unrelated legal expenses. We use, and we believe our investors benefit from, the presentation of Adjusted EBITDA in evaluating our operating performance because it provides us and our investors with additional tools to compare our operating performance on a consistent basis by removing the impact of certain items that management believes do not directly reflect our core operations. In addition, we believe that Adjusted EBITDA is useful to investors and other external users of our consolidated financial statements in evaluating our operating performance as compared to that of other companies, because it allows them to measure a company's operating performance without regard to items such as interest expense, taxes, depreciation and depletion, and amortization and accretion, which can vary substantially from company to company depending upon accounting methods and book value of assets and liabilities, capital structure and the method by which assets were acquired. Our management also uses Adjusted EBITDA for planning purposes, including the preparation of our annual operating budget and financial projections. Management also uses Adjusted EBITDA to evaluate our ability to make certain payments, including dividends, in compliance with our senior credit facilities, which is determined based on a calculation of Consolidated Adjusted EBITDA that is substantially similar to Adjusted EBITDA.

Adjusted EBITDA has limitations as an analytical tool. As a result, you should not consider it in isolation, or as a substitute for net income, operating income, cash flow from operating activities or any other measure of financial performance or liquidity presented in accordance with GAAP. Some of these limitations are:

- Adjusted EBITDA does not reflect our cash expenditures or future requirements for capital expenditures or contractual commitments;
- Adjusted EBITDA does not reflect changes in, or cash requirements for, our working capital needs;

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

- Adjusted EBITDA does not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, on our indebtedness;
- Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future;
- Adjusted EBITDA does not reflect any cash requirements for such replacements;

Table of Contents

- Other companies, including other companies in our industry, may calculate Adjusted EBITDA differently than we do, limiting its usefulness as a comparative measure; and
- Adjusted EBITDA does not reflect tax obligations whether current or deferred.

The following table presents a reconciliation of net income (loss), the most comparable GAAP financial measure, to Adjusted EBITDA as well as the resulting calculation of Adjusted EBITDA for the three and nine months ended September 30, 2010 and 2009:

	Three months ended		Nine months ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Net Income (Loss)	\$ 2,185	\$ 2,738	\$ (3,459)	\$ 3,941
Interest Expense - Net	2,334	3,802	9,038	11,756
Income Taxes	2,279	1,725	(2,803)	751
Depreciation Expense	1,262	1,291	4,827	3,877
Amortization	1,541	1,541	4,621	4,621
EBITDA	9,601	11,097	12,224	24,946
Management Fees	57	411	6,370	1,066
Stock Based Compensation	1,337	6	3,158	738
Loss on Extinguishment of Debt	-	-	7,967	-
Liquidity Bonus Plan	-	-	1,003	-
Other non-recurring charges (1)	565	1,138	1,383	1,286
Adjusted EBITDA	\$ 11,560	\$ 12,652	\$ 32,105	\$ 28,036

(1) Reflects severance and one-time, non-recurring expenses for costs related to the closure of our Johnson City facility of (\$1) and \$872 for the three months and \$828 and \$897 for the nine months ended September 30, 2010 and 2009, respectively, \$566 and \$266 of unrelated legal fees for the three months and \$1,222 and \$389 for the nine months ended September 30, 2010 and 2009 respectively, and \$667 and \$0 gain on other post employment benefit plan curtailment related to the Johnson City plant closure for the nine months ended September 30, 2010 and 2009, respectively.

Discussion of Critical Accounting Policies

For a discussion of our critical accounting policies, please see the disclosure included in the prospectus related to our IPO, filed with the SEC in accordance with Rule 424(b) of the Securities Act, under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operation - Critical Accounting Policies" on May 6, 2010, which is accessible on the SEC's website at www.sec.gov.

New Accounting Pronouncements

For the nine months ended September 30, 2010, the Company did not adopt any new accounting pronouncements that had a significant impact to the Company's consolidated financial statements.

Liquidity and Capital Resources

Our principal sources of cash have been and we expect will continue to be cash from operations and borrowings under our senior credit facilities. As of September 30, 2010, our senior credit facilities consisted of a \$60 million senior secured revolving credit facility, entered into by our subsidiaries, Douglas Dynamics, L.L.C., Douglas Dynamics Finance Company and Fisher, LLC, as borrowers and a \$125 million senior secured term loan facility, entered into by Douglas Dynamics, L.L.C., as borrower, each on May 21, 2007, and as amended on April 16, 2010 in connection with our IPO. Concurrent with the consummation of our IPO, we amended our senior credit facilities to, among other things, (i) allow us to redeem our Senior Notes, (ii) increase the size of our term loan facility by \$40 million from \$85 million to \$125 million, which additional term loans will mature in May 2016 and (iii) amend certain of the provisions in our senior credit facilities which govern our ability to pay dividends. On June 9, 2010, we completed the redemption of our Senior Notes. We redeemed the Senior Notes using the proceeds from our IPO, together with the increase in our term loan facility and cash on hand, for a total of \$157.6 million including the accrued interest thereon and a redemption premium.

Table of Contents

We expect that our primary uses of cash will be to provide working capital, meet debt service requirements, finance capital expenditures, pay dividends under our dividend policy and support our growth, including through potential acquisitions, and for other general corporate purposes. For a description of the seasonality of our working capital rates see Seasonality and Year-To-Year Variability.

As discussed in the prospectus relating to our IPO, in connection with our IPO, our Board of Directors adopted a dividend policy, reflecting an intention to distribute to our stockholders a regular quarterly cash dividend, commencing in the third quarter of 2010 in equal quarterly installments. The initial annual rate for the dividend was \$0.73 per share, or \$0.1825 per quarter, but our Board of Directors has approved a \$0.0175 increase in the fourth quarter 2010 to \$0.20 per share. The declaration and payment of these dividends to holders of our common stock will be at the discretion of our Board of Directors and will depend upon many factors, including our financial condition and earnings, legal requirements, taxes and other factors our Board of Directors may deem to be relevant. The terms of our indebtedness also restricts us from paying cash dividends on our common stock under certain circumstances. As a result of this dividend policy, we may not have significant cash available to meet any large unanticipated liquidity requirements. As a result, we may not retain a sufficient amount of cash to fund our operations or to finance unanticipated capital expenditures or growth opportunities, including acquisitions. Our Board of Directors may, however, amend, revoke or suspend our dividend policy at any time and for any reason.

As of September 30, 2010, we had \$31.7 million of total liquidity, comprised of \$8.7 million in cash and cash equivalents and borrowing availability of \$23.0 million under our revolving credit facility. Borrowing availability under our revolving credit facility is governed by a borrowing base, the calculation of which includes cash on hand. Accordingly, use of cash on hand may also result in a reduction in the amount available for borrowing under our revolving credit facility. Furthermore, our revolving credit facility requires us to maintain at least \$6.0 million of borrowing availability. We expect that cash on hand, generated from operations, as well as available credit under our senior credit facilities will provide adequate funds for the purposes described above for at least the next 12 months.

The following table shows our cash and cash equivalents and inventories in thousands at September 30, 2010, December 31, 2009 and September 30, 2009.

	As of		
	September 30, 2010	December 31, 2009	September 30, 2009
Cash and cash equivalents	\$ 8,721	\$ 69,703	\$ 17,210
Inventories	24,475	26,697	26,853

We had cash and cash equivalents of \$8.7 million at September 30, 2010 compared to cash and cash equivalents of \$17.2 million at September 30, 2009. The table below sets forth a summary of the significant sources and uses of cash for the periods presented in thousands.

Cash Flows (in thousands)	Nine months ended September 30,		Change	% Change
	2010	2009		
Net cash provided by (used in) operating activities	\$ (38,435)	\$ (39,883)	\$ 1,448	(3.6)%
Net cash provided by (used in) investing activities	(2,202)	(4,821)	2,619	(54.3)%
Net cash provided by (used in) financing activities	(19,715)	8,362	(28,077)	(335.8)%

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

Increase (Decrease) in cash	\$	(60,352)	\$	(36,342)	\$	(24,010)	66.1%
-----------------------------	----	----------	----	----------	----	----------	-------

Net cash used in operating activities decreased \$1.4 million from the nine months ended September 30, 2009 to the nine months ended September 30, 2010. This decrease in cash used was driven mainly by a year over year increase in pre-tax gross profit of \$4.6 million driven by increased unit shipments and improved unit margins, as well as decreased interest expense. Partially offsetting this were non-recurring costs incurred at the time of the Company IPO, namely the buyout of the management services agreement totaling \$5.8 million, and the payment of cash bonuses under the Company's liquidity bonus plan totaling \$1.0 million.

Table of Contents

Net cash used in investing activities decreased \$2.6 million for the nine months ended September 30, 2010, compared to the corresponding period in 2009. This decrease was driven largely by the purchase of a Milwaukee distribution facility during the second quarter of 2009 to expand our Milwaukee facilities in anticipation of the closure of our Johnson City, TN manufacturing plant.

Net cash used in financing activities increased \$28.0 million for the nine months ended September 30, 2010 compared to the corresponding period in 2009, primarily as a result of the net impact of financing activities associated with the Company's IPO, namely the redemption of the Company's Senior Notes, including the redemption premium and accrued interest thereon totaling \$153.9 million, partially offset by an increase in our term loan of \$40.0 million, net proceeds from the IPO of \$63.9 million, and revolver borrowings of \$37.0 million.

Contractual Obligations

There have been no material changes to our contractual obligations in the nine months ended September 30, 2010, except for (a) a reduction in long-term debt and related interest obligations as a result of the redemption of our Senior Notes on June 9, 2010 and (b) an increase in our term loan facility by \$40 million to \$125 million. For additional details regarding the changes to our long-term debt, see Note 5 to the notes to our consolidated financial statements.

Off-Balance Sheet Arrangements

We are not party to any off-balance sheet arrangements that have or are reasonably likely to have a material current or future effect on our financial condition, changes in financial condition, revenues, expenses, results of operations, liquidity, capital expenditures or capital resources.

Seasonality and Year-to-Year Variability

Our business is seasonal and also varies from year-to-year. Consequently, our results of operations and financial condition vary from quarter-to-quarter and from year-to-year as well. In addition, because of this seasonality and variability, our results of operations for any quarter may not be indicative of results of operations that may be achieved for a subsequent quarter or the full year, and may not be similar to results of operations experienced in prior years. That being the case, while snowfall levels vary within a given year and from year-to-year, snowfall, and the corresponding replacement cycle of snow and ice control equipment, is relatively consistent over multi-year periods.

Sales of our products are significantly impacted by the level, timing and location of snowfall, with sales in any given year and region most heavily influenced by snowfall levels in the prior snow season (which we consider to begin in October and end in March) in that region. This is due to the fact that end-user demand for our products is driven primarily by the condition of their snow and ice control equipment, and in the case of professional snowplowers, by their financial ability to purchase new or replacement snow and ice control equipment, both of which are significantly affected by snowfall levels. Heavy snowfall during a given winter causes usage of our products to increase, resulting in greater wear and tear to our products and a shortening of their life cycles, thereby creating a need for replacement snow and ice control equipment and related parts and accessories. In addition, when there is a heavy snowfall in a given winter, the increased income our professional snowplowers generate from their professional snowplow activities provides them with increased purchasing power to purchase replacement snow and ice

control equipment prior to the following winter. To a lesser extent, sales of our products are influenced by the timing of snowfall in a given winter. Because an early snowfall can be viewed as a sign of a heavy upcoming snow season, our end-users may respond to an early snowfall by purchasing replacement snow and ice control equipment during the current season rather than delaying purchases until after the season is over when most purchases are typically made by end-users.

We attempt to manage the seasonal impact of snowfall on our revenues in part through our pre-season sales program, which involves actively soliciting and encouraging pre-season distributor orders in the second and third quarters by offering our distributors a combination of pricing, payment and freight incentives during this period. These pre-season sales incentives encourage our distributors to re-stock their inventory during the second and third quarters in anticipation of the peak fourth quarter retail sales period by offering pre-season pricing and payment deferral until the fourth quarter. As a result, we tend to generate our greatest volume of sales (an average of over two-thirds over the last ten years) during the second and third quarters, providing us with manufacturing visibility for the remainder of the year. By contrast, our revenue and operating results tend to be lowest during the first quarter as management believes our end-users prefer to wait until the beginning of a snow season to purchase new equipment and as our distributors sell off inventory and wait for our pre-season sales incentive period to re-stock inventory. Fourth quarter sales vary from year-to-year as they are primarily driven by the level, timing and location of snowfall during the quarter. This is because most of our fourth quarter sales and shipments consist of re-orders by distributors seeking to restock inventory to meet immediate customer needs caused by snowfall during the winter months.

Table of Contents

Because of the seasonality of our sales, we experience seasonality in our working capital needs as well. In the first quarter we typically require capital as we are generally required to build our inventory in anticipation of our second and third quarter pre-season sales. During the second and third quarters, our working capital requirements rise as our accounts receivable increase as a result of the sale and shipment of products ordered through our pre-season sales program and we continue to build inventory. Working capital requirements peak towards the end of the third quarter and then begin to decline through the fourth quarter through a reduction in accounts receivable when we receive the majority of the payments for pre-season shipped products.

We also attempt to manage the impact of seasonality and year-to-year variability on our business costs through the effective management of our assets. Our asset management and profit focus strategies include:

- the employment of a highly variable cost structure facilitated by a core group of workers that we supplement with a temporary workforce as sales volumes dictate, which allows us to adjust costs on an as-needed basis in response to changing demand;
- our enterprise-wide lean concept, which allows us to adjust production levels up or down to meet demand;
- the pre-season order program described above, which incentivizes distributors to place orders prior to the retail selling season; and
- a vertically integrated business model.

These asset management and profit focus strategies, among other management tools, allow us to adjust fixed overhead and sales, general and administrative expenditures to account for the year-to-year variability of our sales volumes.

Additionally, although modest, our annual capital expenditure requirements can be temporarily reduced by up to approximately 40% in response to actual or anticipated decreases in sales volumes. If we are unsuccessful in our asset management initiatives, the seasonality and year-to-year variability effects on our business may be compounded and in turn our results of operations and financial condition may suffer.

Item 3. *Quantitative and Qualitative Disclosures About Market Risk*

We do not use financial instruments for speculative trading purposes, and do not hold any derivative financial instruments that could expose us to significant market risk. Our primary market risk exposures are changes in interest rates and steel price fluctuations.

Interest Rate Risk

We are exposed to market risk primarily from changes in interest rates. Certain of our borrowings, including our term loan and any revolving borrowings under our senior credit facilities, are at variable rates of interest and expose us to interest rate risk. In addition, the interest rate on

any revolving borrowings is subject to an increase in the interest rate based on our average daily availability under our revolving credit facility. When the average daily excess availability on our revolving credit facility falls below \$25 million, our interest rate on the revolving credit facility will increase by 0.25%. The maximum impact this would have on our interest expense would be \$150,000 per year. If interest rates increase, our debt service obligations on our variable rate indebtedness would increase even though the amount borrowed remained the same, and our net income and cash flows would correspondingly decrease.

As of September 30, 2010, we had outstanding borrowings under our term loan of \$121.8 million. A hypothetical interest rate change of 1%, 1.5% and 2% on our term loan would have changed interest incurred for the nine months ended September 30, 2010 by \$0.3 million, \$0.4 million and \$0.7 million, respectively. As of September 30, 2010, we had outstanding borrowings under our revolving credit facility of \$37.0 million. A hypothetical interest rate change of 1%, 1.5% and 2% on our revolving credit facility would have changed interest incurred for the nine months ended September 30, 2010 by \$0.1 million, \$0.1 million and \$0.2 million, respectively.

Commodity Price Risk

In the normal course of business, we are exposed to market risk related to our purchase of steel, the primary commodity upon which our manufacturing depends. Our steel purchases as a percentage of revenue were 15.5% and 18.1% for the nine months ended September 30, 2010 and 2009, respectively. While steel is typically available from numerous suppliers, the price of steel is a commodity subject to fluctuations that apply across broad spectrums of the steel market. We do not use any derivative or hedging instruments to manage steel price risk. If the price of steel increases, our variable costs could also increase. While historically we have successfully mitigated these increased costs through the implementation of either permanent price increases and/or temporary invoice surcharges, in the future we may not be able to successfully mitigate these costs, which could cause our gross margins to decline. If our costs for steel were to increase by \$1.00 in a period where we are not able to pass any of this increase onto our distributors, our gross margins would decline by \$1.00 in the period in which such inventory was sold.

Table of Contents

Item 4. Controls And Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that as of the end of the period covered by this Quarterly Report our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and include controls and procedures designed to ensure that the information required to be disclosed by us in such reports is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

Changes in Internal Control Over Financial Reporting

There have been no changes in the Company's internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In the ordinary course of business, we are engaged in various litigation primarily including product liability and intellectual property disputes. However, management does not believe that any current litigation is material to our operations or financial position. In addition, we are not currently party to any environmental-related claims or legal matters.

Item 1A. Risk Factors

The Company operates in an environment that involves numerous known and unknown risks and uncertainties. Our business, prospects, financial condition and operating results could be materially adversely affected by any of these risks, as well as other risks not currently known to us or that we currently consider immaterial. The risks described below highlight some of the factors that have affected, and in the future could affect our operations.

Our results of operations depend primarily on the level, timing and location of snowfall. As a result, a decline in snowfall levels in multiple regions for an extended time could cause our results of operations to decline and adversely affect our ability to pay dividends.

As a manufacturer of snow and ice control equipment for light trucks, and related parts and accessories, our sales depend primarily on the level, timing and location of snowfall in the regions in which we offer our products. A low level or lack of snowfall in any given year in any of the snowbelt regions in North America (primarily the Midwest, East and Northeast regions of the United States as well as all provinces of Canada) will likely cause sales of our products to decline in such year as well as the subsequent year, which in turn may adversely affect our results of operations and ability to pay dividends. See Management's Discussion and Analysis of Financial Condition and Results of Operations Seasonality and Year-to-Year Variability. A sustained period of reduced snowfall events in one or more of the geographic regions in which we offer our products could cause our results of operations to decline and adversely affect our ability to pay dividends.

The year-to-year variability of our business can cause our results of operations and financial condition to be materially different from year-to-year; whereas the seasonality of our business can cause our results of operations and financial condition to be materially different from quarter-to-quarter.

Because our business depends on the level, timing and location of snowfall, our results of operations vary from year-to-year. Additionally, because the annual snow season typically only runs from October 1 through March 31, our distributors typically purchase our products during the second and third quarters. As a result, we operate in a seasonal business. We not only experience seasonality in our sales, but also experience seasonality in our working capital needs. Consequently, our results of operations and financial condition can vary from year-to-year, as well as from quarter-to-quarter, which could affect our ability to pay dividends. If we are unable to effectively manage the seasonality and year-to-year variability of our business, our results of operations, financial condition and ability to pay dividends may suffer.

Table of Contents

If economic conditions in the United States continue to remain weak or deteriorate further, our results of operations, financial condition and ability to pay dividends may be adversely affected.

Historically, demand for snow and ice control equipment for light trucks has been influenced by general economic conditions in the United States, as well as local economic conditions in the snowbelt regions in North America. During the last few years, economic conditions throughout the United States have been extremely weak, and may not improve in the foreseeable future. Weakened economic conditions may cause our end-users to delay purchases of replacement snow and ice control equipment and instead repair their existing equipment, leading to a decrease in our sales of new equipment. Weakened economic conditions may also cause our end-users to delay their purchases of new light trucks. Because our end-users tend to purchase new snow and ice control equipment concurrent with their purchase of new light trucks, their delay in purchasing new light trucks can also result in the deferral of their purchases of new snow and ice control equipment. The deferral of new equipment purchases during periods of weak economic conditions may negatively affect our results of operations, financial condition and ability to pay dividends.

Weakened economic conditions may also cause our end-users to consider price more carefully in selecting new snow and ice control equipment. Historically, considerations of quality and service have outweighed considerations of price, but in a weak economy, price may become a more important factor. Any refocus away from quality in favor of cheaper equipment could cause end-users to shift away from our products to less expensive competitor products, or to shift away from our more profitable products to our less profitable products, which in turn would adversely affect our results of operations and our ability to pay dividends.

Our failure to maintain good relationships with our distributors, the loss or consolidation of our distributor base or the actions or inactions of our distributors could have an adverse effect on our results of operations and our ability to pay dividends.

We depend on a network of truck equipment distributors to sell, install and service our products. Nearly all of these sales and service relationships are at will, and less than 1% of our distributors have agreed not to offer products that compete with our products. As a result, almost all of our distributors could discontinue the sale and service of our products at any time, and those distributors that primarily sell our products may choose to sell competing products at any time. Further, difficult economic or other circumstances could cause any of our distributors to discontinue their businesses. Moreover, if our distributor base were to consolidate or if any of our distributors were to discontinue their business, competition for the business of fewer distributors would intensify. If we do not maintain good relationships with our distributors, or if we do not provide product offerings and pricing that meet the needs of our distributors, we could lose a substantial amount of our distributor base. A loss of a substantial portion of our distributor base could cause our sales to decline significantly, which would have an adverse effect on our results of operations and ability to pay dividends.

In addition, our distributors may not provide timely or adequate service to our end-users. If this occurs, our brand identity and reputation may be damaged, which would have an adverse effect on our results of operations and ability to pay dividends.

Lack of available financing options for our end-users or distributors may adversely affect our sales volumes.

Our end-user base is highly concentrated among professional snowplowers, who comprise over 50% of our end-users, many of whom are individual landscapers who remove snow during the winter and landscape during the rest of the year, rather than large, well-capitalized

corporations. These end-users often depend upon credit to purchase our products. If credit is unavailable on favorable terms or at all, our end-users may not be able to purchase our products from our distributors, which would in turn reduce sales and adversely affect our results of operations and ability to pay dividends.

In addition, because our distributors, like our end-users, rely on credit to purchase our products, if our distributors are not able to obtain credit, or access credit on favorable terms, we may experience delays in payment or nonpayment for delivered products. Further, if our distributors are unable to obtain credit or access credit on favorable terms, they could experience financial difficulties or bankruptcy and cease purchases of our products altogether. Thus, if financing is unavailable on favorable terms or at all, our results of operations and ability to pay dividends would be adversely affected.

The price of steel, a commodity necessary to manufacture our products, is highly variable. If the price of steel increases, our gross margins could decline.

Steel is a significant raw material used to manufacture our products. During 2007, 2008 and 2009, our steel purchases were approximately 12%, 15% and 18% of our revenue, respectively. The steel industry is highly cyclical in nature, and steel prices have been volatile in recent years and may remain volatile in the future. Steel prices are influenced by numerous factors beyond our control, including general economic conditions domestically and internationally, the availability of raw materials, competition, labor costs,

Table of Contents

freight and transportation costs, production costs, import duties and other trade restrictions. After experiencing a downward trend in steel prices throughout most of 2009, steel prices may increase as a result of increased demand from the automobile and consumer durable sectors. If the price of steel increases, our variable costs may increase. We may not be able to mitigate these increased costs through the implementation of permanent price increases or temporary invoice surcharges, especially if economic conditions remain weak and our distributors and end-users become more price sensitive. If we are unable to successfully mitigate such cost increases in the future, our gross margins could decline.

We depend on outside suppliers who may be unable to meet our volume and quality requirements, and we may be unable to obtain alternative sources.

We purchase certain components essential to our snowplows and sand and salt spreaders from outside suppliers, including off-shore sources. Most of our key supply arrangements can be discontinued at any time. A supplier may encounter delays in the production and delivery of such products and components or may supply us with products and components that do not meet our quality, quantity or cost requirements. Additionally, a supplier may be forced to discontinue operations. Any discontinuation or interruption in the availability of quality products and components from one or more of our suppliers may result in increased production costs, delays in the delivery of our products and lost end-user sales, which could have an adverse effect on our business and financial condition.

In addition, we have begun to increase the number of our off-shore suppliers. Our increased reliance on off-shore sourcing may cause our business to be more susceptible to the impact of natural disasters, war and other factors that may disrupt the transportation systems or shipping lines used by our suppliers, a weakening of the dollar over an extended period of time and other uncontrollable factors such as changes in foreign regulation or economic conditions. In addition, reliance on off-shore suppliers may make it more difficult for us to respond to sudden changes in demand because of the longer lead time to obtain components from off-shore sources. We may be unable to mitigate this risk by stocking sufficient materials to satisfy any sudden or prolonged surges in demand for our products. If we cannot satisfy demand for our products in a timely manner, our sales could suffer as distributors can cancel purchase orders without penalty until shipment.

We do not sell our products under long-term purchase contracts, and sales of our products are significantly impacted by factors outside of our control; therefore, our ability to estimate demand is limited.

We do not enter into long-term purchase contracts with our distributors and the purchase orders we receive may be cancelled without penalty until shipment. Therefore, our ability to accurately predict future demand for our products is limited. Nonetheless, we attempt to estimate demand for our products for purposes of planning our annual production levels and our long-term product development and new product introductions. We base our estimates of demand on our own market assessment, snowfall figures, quarterly field inventory surveys and regular communications with our distributors. Because wide fluctuations in the level, timing and location of snowfall, economic conditions and other factors may occur, each of which is out of our control, our estimates of demand may not be accurate. Underestimating demand could result in procuring an insufficient amount of materials necessary for the production of our products, which may result in increased production costs, delays in product delivery, missed sale opportunities and a decrease in customer satisfaction. Overestimating demand could result in the procurement of excessive supplies, which could result in increased inventory and associated carrying costs.

If we are unable to enforce, maintain or continue to build our intellectual property portfolio, or if others invalidate our intellectual property rights, our competitive position may be harmed.

We rely on a combination of patents, trade secrets and trademarks to protect certain of the proprietary aspects of our business and technology. We hold approximately 20 U.S. registered trademarks (including the trademarks WESTERN®, FISHER® and BLIZZARD®), 5 Canadian registered trademarks, 28 U.S. issued patents and 15 Canadian patents. Although we work diligently to protect our intellectual property rights, monitoring the unauthorized use of our intellectual property is difficult, and the steps we have taken may not prevent unauthorized use by others. In addition, in the event a third party challenges the validity of our intellectual property rights, a court may determine that our intellectual property rights may not be valid or enforceable. An adverse determination with respect to our intellectual property rights may harm our business prospects and reputation. Third parties may design around our patents or may independently develop technology similar to our trade secrets. The failure to adequately build, maintain and enforce our intellectual property portfolio could impair the strength of our technology and our brands, and harm our competitive position. Although the Company has no reason to believe that its intellectual property rights are vulnerable, previously undiscovered intellectual property could be used to invalidate our rights.

Table of Contents

If we are unable to develop new products or improve upon our existing products on a timely basis, it could have an adverse effect on our business and financial condition.

We believe that our future success depends, in part, on our ability to develop on a timely basis new technologically advanced products or improve upon our existing products in innovative ways that meet or exceed our competitors' product offerings. Continuous product innovation ensures that our consumers have access to the latest products and features when they consider buying snow and ice control equipment. Maintaining our market position will require us to continue to invest in research and development and sales and marketing. Product development requires significant financial, technological and other resources. We may be unsuccessful in making the technological advances necessary to develop new products or improve our existing products to maintain our market position. Industry standards, end-user expectations or other products may emerge that could render one or more of our products less desirable or obsolete. If any of these events occur, it could cause decreases in sales, a failure to realize premium pricing and an adverse effect on our business and financial condition.

We face competition from other companies in our industry, and if we are unable to compete effectively with these companies, it could have an adverse effect on our sales and profitability. Price competition among our distributors could negatively affect our market share.

We primarily compete with regional manufacturers of snow and ice control equipment for light trucks. While we are the most geographically diverse company in our industry, we may face increasing competition in the markets in which we operate. In saturated markets, price competition may lead to a decrease in our market share or a compression of our margins, both of which would affect our profitability. Moreover, current or future competitors may grow their market share and develop superior service and may have or may develop greater financial resources, lower costs, superior technology or more favorable operating conditions than we maintain. As a result, competitive pressures we face may cause price reductions for our products, which would affect our profitability or result in decreased sales and operating income. Additionally, saturation of the markets in which we compete or channel conflicts among our brands and shifts in consumer preferences may increase these competitive pressures or may result in increased competition among our distributors and affect our sales and profitability. In addition, price competition among the distributors that sell our products could lead to significant margin erosion among our distributors, which could in turn result in compressed margins or loss of market share for us. Management believes that after Douglas, the next largest competitors in the market for snow and ice control equipment for light trucks are BOSS and Meyer, respectively, and accordingly represent our primary competitors for market share.

We are subject to complex laws and regulations, including environmental and safety regulations, that can adversely affect the cost, manner or feasibility of doing business.

Our operations are subject to certain federal, state and local laws and regulations relating to, among other things, the generation, storage, handling, emission, transportation, disposal and discharge of hazardous and non-hazardous substances and materials into the environment, the manufacturing of motor vehicle accessories and employee health and safety. We cannot be certain that existing and future laws and regulations and their interpretations will not harm our business or financial condition. We currently make and may be required to make large and unanticipated capital expenditures to comply with environmental and other regulations, such as:

- applicable motor vehicle safety standards established by the National Highway Traffic Safety Administration;
- reclamation and remediation and other environmental protection; and

- standards for workplace safety established by the Occupational Safety and Health Administration.

While we monitor our compliance with applicable laws and regulations and attempt to budget for anticipated costs associated with compliance, we cannot predict the future cost of such compliance. During 2009 we expended approximately \$450,000 related to compliance with such regulations and could expend similar or greater amounts in the future in the event of future legislation changes or unforeseen events, such as a workplace accident or environmental discharge, or if we otherwise discover we are in non-compliance with an applicable regulation. In addition, under these laws and regulations, we could be liable for:

- product liability claims;
- personal injuries;
- investigation and remediation of environmental contamination and other governmental sanctions such as fines and penalties; and
- other environmental damages.

Our operations could be significantly delayed or curtailed and our costs of operations could significantly increase as a result of regulatory requirements, restrictions or claims. We are unable to predict the ultimate cost of compliance with these requirements or their effect on our operations.

Table of Contents

Financial market conditions have had a negative impact on the return on plan assets for our pension plans, which may require additional funding and negatively impact our cash flows.

Our pension expense and required contributions to our pension plan are directly affected by the value of plan assets, the projected rate of return on plan assets, the actual rate of return on plan assets and the actuarial assumptions we use to measure the defined benefit pension plan obligations. Due to the significant financial market downturn during 2008, the funded status of our pension plans has declined. As of December 31, 2009, our pension plans were underfunded by approximately \$9 million. In 2009, contributions to our defined benefit pension plans were approximately \$1.4 million. If plan assets continue to perform below expectations, future pension expense and funding obligations will increase, which would have a negative impact on our cash flows. Moreover, under the Pension Protection Act of 2006, it is possible that continued losses of asset values may necessitate accelerated funding of our pension plans in the future to meet minimum federal government requirements.

The statements regarding our industry, market positions and market share in this report are based on our management's estimates and assumptions. While we believe such statements are reasonable, such statements have not been independently verified.

Information contained in this report concerning the snow and ice control equipment industry for light trucks, our general expectations concerning this industry and our market positions and other market share data regarding the industry are based on estimates our management prepared using end-user surveys, anecdotal data from our distributors and distributors that carry our competitors' products, our results of operations and management's past experience, and on assumptions made, based on our management's knowledge of this industry, all of which we believe to be reasonable. These estimates and assumptions are inherently subject to uncertainties, especially given the year-to-year variability of snowfall and the difficulty of obtaining precise information about our competitors, and may prove to be inaccurate. In addition, we have not independently verified the information from any third-party source and thus cannot guarantee its accuracy or completeness, although management also believes such information to be reasonable. Our actual operating results may vary significantly if our estimates and outlook concerning the industry, snowfall patterns, our market positions or our market shares turn out to be incorrect.

We are subject to product liability claims, product quality issues, and other litigation from time to time that could adversely affect our operating results or financial condition.

The manufacture, sale and usage of our products expose us to a risk of product liability claims. If our products are defective or used incorrectly by our end-users, injury may result, giving rise to product liability claims against us. If a product liability claim or series of claims is brought against us for uninsured liabilities or in excess of our insurance coverage, and it is ultimately determined that we are liable, our business and financial condition could suffer. Any losses that we may suffer from any liability claims, and the effect that any product liability litigation may have upon the reputation and marketability of our products, may divert management's attention from other matters and may have a negative impact on our business and operating results. Additionally, we could experience a material design or manufacturing failure in our products, a quality system failure or other safety issues, or heightened regulatory scrutiny that could warrant a recall of some of our products. A recall of some of our products could also result in increased product liability claims. Any of these issues could also result in loss of market share, reduced sales, and higher warranty expense.

We are heavily dependent on our Chief Executive Officer and management team.

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

Our continued success depends on the retention, recruitment and continued contributions of key management, finance, sales and marketing personnel, some of whom could be difficult to replace. Our success is largely dependent upon our senior management team, led by our Chief Executive Officer and other key managers. The loss of any one or more of such persons could have an adverse effect on our business and financial condition.

Our indebtedness could adversely affect our operations, including our ability to perform our obligations and pay dividends.

As of September 30, 2010 we had approximately \$121.8 million of senior secured indebtedness and \$23.0 million of borrowing availability under our revolving credit facility. We may also be able to incur substantial indebtedness in the future, including senior indebtedness, which may or may not be secured.

Our indebtedness could have important consequences to our stockholders, including the following:

- we could have difficulty satisfying our debt obligations, and if we fail to comply with these requirements, an event of default could result;
- we may be required to dedicate a substantial portion of our cash flow from operations to required payments on indebtedness, thereby reducing the cash flow available to pay dividends or fund working capital, capital expenditures and other general corporate activities;

Table of Contents

- covenants relating to our indebtedness may restrict our ability to make dividends or distributions to our stockholders;
- covenants relating to our indebtedness may limit our ability to obtain additional financing for working capital, capital expenditures and other general corporate activities, which may limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- we may be more vulnerable to general adverse economic and industry conditions;
- we may be placed at a competitive disadvantage compared to our competitors with less debt; and
- we may have difficulty repaying or refinancing our obligations under our senior credit facilities on their respective maturity dates.

If any of these consequences occur, our financial condition, results of operations and ability to pay dividends could be adversely affected. This, in turn, could negatively affect the market price of our common stock, and we may need to undertake alternative financing plans, such as refinancing or restructuring our debt, selling assets, reducing or delaying capital investments or seeking to raise additional capital. We cannot assure you that any refinancing would be possible, that any assets could be sold, or, if sold, of the timing of the sales and the amount of proceeds that may be realized from those sales, or that additional financing could be obtained on acceptable terms, if at all.

Our variable rate indebtedness subjects us to interest rate risk, which could cause our debt service obligations to increase significantly and could impose adverse consequences.

Certain of our borrowings, including our term loan and any revolving borrowings under our senior credit facilities, are at variable rates of interest and expose us to interest rate risk. In addition, the interest rate on any revolving borrowings is subject to an increase in the interest rate if the average daily availability under our revolving credit facility falls below a certain threshold. If interest rates increase, our debt service obligations on the variable rate indebtedness would increase even though the amount borrowed remained the same, and our net income and cash flows would correspondingly decrease.

Our senior credit facilities impose restrictions on us, which may also prevent us from capitalizing on business opportunities and taking certain corporate actions. One of these facilities also includes minimum availability requirements, which if unsatisfied, could result in liquidity events that may jeopardize our business.

Our senior credit facilities contain, and future debt instruments to which we may become subject may contain, covenants that limit our ability to engage in activities that could otherwise benefit our company, including restrictions on our ability to:

- incur, assume or permit to exist additional indebtedness or contingent obligations;
- incur liens and engage in sale and leaseback transactions;
- make loans and investments in excess of agreed upon amounts;
- declare dividends, make payments or redeem or repurchase capital stock in excess of agreed upon amounts and subject to certain other limitations;
- engage in mergers, acquisitions and other business combinations;
- prepay, redeem or purchase certain indebtedness or amend or alter the terms of our indebtedness;
- sell assets;
- transact with affiliates or our stockholders; and
- alter the business that we conduct.

Our revolving credit facility also includes limitations on capital expenditures and requires us to maintain at least \$6 million of borrowing availability. Failure to maintain such availability would constitute a liquidity event under our revolving credit facility, and as a result we would be required to comply with a fixed charge coverage ratio test. In addition, if such a liquidity event (or an event of default) occurs and is continuing, subject to certain limited cure rights, all proceeds of our accounts receivable and other collateral will be applied to reduce obligations under our revolving credit facility, jeopardizing our ability to meet other obligations. Our ability to comply with the covenants contained in our senior credit facilities or in the agreements governing our future indebtedness, and our ability to avoid liquidity events, may be affected by events, or our future performance, which are subject to factors beyond our control, including prevailing economic, financial, industry and weather conditions, such as the level, timing and location of snowfall and general economic conditions in the snowbelt regions of North America. A failure to comply with these

Table of Contents

covenants could result in a default under our senior credit facilities, which could prevent us from paying dividends, borrowing additional amounts and using proceeds of our inventory and accounts receivable, and also permit the lenders to accelerate the payment of such debt. If any of our debt is accelerated or if a liquidity event (or event of default) occurs that results in collateral proceeds being applied to reduce such debt, we may not have sufficient funds available to repay such debt and our other obligations, in which case, our business could be halted and such lenders could proceed against any collateral securing that debt. Further, if the lenders accelerate the payment of the indebtedness under our senior credit facilities, our assets may not be sufficient to repay in full the indebtedness under our senior credit facilities and our other indebtedness, if any. We cannot assure you that these covenants will not adversely affect our ability to finance our future operations or capital needs to pursue available business opportunities or react to changes in our business and the industry in which we operate.

The closure of our Johnson City, Tennessee manufacturing facility may entail risks to our business.

As part of our lean manufacturing strategy to lower our fixed costs, we closed our Johnson City, Tennessee manufacturing facility in the third quarter ending September 30, 2010 and thereby reduced our manufacturing facilities from three to two. In connection with this closure, we relocated our Johnson City operations and equipment into our remaining two facilities. We cannot assure you that we will realize contemplated cost savings from the closure of this facility. In addition, there may be risks associated with this closure for which we are unprepared, such as labor and employment litigation, difficulties implementing a smooth transition and the possibility that this closure leaves us with insufficient manufacturing capacity. It is therefore possible that our business could be negatively affected by the closure of this facility.

Our principal stockholders hold a significant portion of our common stock and may have different interests than us or you in the future.

Our principal stockholders have the right to vote or direct the vote of approximately 46% of our voting power. Consequently, our principal stockholders will for the foreseeable future be able to influence the election and removal of our directors and influence our corporate and management policies, including virtually all matters requiring stockholder approval, such as potential mergers or acquisitions, asset sales and other significant corporate transactions. This concentration of ownership may delay or deter possible changes in control of the Company. We cannot assure you that the interests of our principal stockholders will coincide with the interests of our other holders of common stock.

Provisions of Delaware law and our charter documents could delay or prevent an acquisition of us, even if the acquisition would be beneficial to you.

Provisions in our certificate of incorporation and bylaws may have the effect of delaying or preventing a change of control or changes in our management. These provisions include:

- the absence of cumulative voting in the election of our directors, which means that the holders of a majority of our common stock may elect all of the directors standing for election;
- the ability of our Board of Directors to issue preferred stock with voting rights or with rights senior to those of our common stock without any further vote or action by the holders of our common stock;

Edgar Filing: DOUGLAS DYNAMICS, INC - Form 10-Q

- the division of our Board of Directors into three separate classes serving staggered three-year terms;
- the ability of our stockholders to remove our directors is limited to cause and only by the vote of at least 66²/₃% of the outstanding shares of our common stock;
- the prohibition on our stockholders from acting by written consent and calling special meetings;
- the requirement that our stockholders provide advance notice when nominating our directors or proposing business to be considered by the stockholders at an annual meeting of stockholders; and
- the requirement that our stockholders must obtain a 66²/₃% vote to amend or repeal certain provisions of our certificate of incorporation.

We are also subject to Section 203 of the Delaware General Corporation Law, which, subject to certain exceptions, prohibits us from engaging in any business combination with any interested stockholder, as defined in that section, for a period of three years following the date on which that stockholder became an interested stockholder. This provision, together with the provisions discussed above, could also make it more difficult for you and our other stockholders to elect directors and take other corporate actions, and could limit the price that investors might be willing to pay in the future for shares of our common stock.

Table of Contents

If we are unable to assess favorably the effectiveness of our internal control over financial reporting, or if our independent registered public accounting firm is unable to provide an unqualified attestation report on our internal controls, our stock price could be adversely affected.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 and the related rules adopted by the SEC and the Public Company Accounting Oversight Board, beginning with our Annual Report on Form 10-K for the year ending 2011, our management will be required to report on, and our independent registered public accounting firm to attest to, the effectiveness of our internal control over financial reporting. We may encounter problems or delays in completing the implementation of any changes necessary to make a favorable assessment of our internal control over financial reporting. In addition, in connection with the attestation process by our independent registered public accounting firm, we may encounter problems or delays in completing the implementation of any requested improvements and receiving a favorable attestation. If we cannot timely and favorably assess the effectiveness of our internal control over financial reporting, or if our independent registered public accounting firm is unable to provide an unqualified attestation report on our internal control over financial reporting, investor confidence and our stock price could decline.

Our dividend policy may limit our ability to pursue growth opportunities.

If we pay dividends at the level currently anticipated under our dividend policy, we may not retain a sufficient amount of cash to finance growth opportunities, meet any large unanticipated liquidity requirements or fund our operations in the event of a significant business downturn. In addition, because a significant portion of cash available will be distributed to holders of our common stock under our dividend policy, our ability to pursue any material expansion of our business, including through acquisitions, increased capital spending or other increases of our expenditures, will depend more than it otherwise would on our ability to obtain third party financing. We cannot assure you that such financing will be available to us at all, or at an acceptable cost. If we are unable to take timely advantage of growth opportunities, our future financial condition and competitive position may be harmed, which in turn may adversely affect the market price of our common stock.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Unregistered Sales of Equity Securities

During the three months ended September 30, 2010, the Company sold no securities that were not registered under the Securities Act of 1933, as amended.

Dividend Payment Restrictions

The Company's senior credit facilities include certain restrictions on its ability to pay dividends. The senior credit facilities also restrict the Company's subsidiaries from paying dividends and otherwise transferring assets to Douglas Dynamics, Inc. For additional detail regarding these restrictions, see Note 5 to the notes to the consolidated financial statements.

Table of Contents

Item 3. Defaults Upon Senior Securities

None.

Item 4. (Removed and Reserved)

Item 5. Other Information

None.

Item 6. Exhibits

The following documents are filed as Exhibits to this Quarterly Report on Form 10-Q:

Exhibit Numbers	Description
10.1	Douglas Dynamics, Inc. 2010 Amended and Restated Stock Incentive Plan (incorporated by reference to Exhibit 99.1 to the Company's Registration Statement on Form S-8 (Registration No. 333-169342) filed with the Securities and Exchange Commission on September 13, 2010)
31.1*	Certification of the Company's Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of the Company's Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of the Company's Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Filed herewith.

[Table of Contents](#)

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

DOUGLAS DYNAMICS, INC.

By: /s/ ROBERT MCCORMICK
Robert McCormick
Executive Vice President and Chief Financial Officer
(Principal Financial Officer and Authorized
Signatory)

Dated: November 8, 2010

Table of Contents

Exhibit Index to Form 10-Q for the Period Ended September 30, 2010

Exhibit Numbers	Description
10.1	Douglas Dynamics, Inc. 2010 Amended and Restated Stock Incentive Plan (incorporated by reference to Exhibit 99.1 to the Company's Registration Statement on Form S-8 (Registration No. 333-169342) filed with the Securities and Exchange Commission on September 13, 2010)
31.1*	Certification of the Company's Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of the Company's Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of the Company's Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Filed herewith.